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GENEVA FOR DEPUTY USTR ALLGEIER

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SUBJECT: SCENESETTER FOR DEPUTY USTR ALLGEIER'S VISIT TO
ETHIOPIA

¶1. (SBU) SUMMARY: Welcome to Addis Ababa! Your visit comes as the country is focused primarily on the recent military operation in Somalia, but Ethiopia is making progress on development through growth and diversification of exports and substantial advances in education and health care. Septel discusses in more detail the GOE's recent submission of its long-delayed Memorandum of Foreign Trade Regime (MFTR) -- an important step in getting the country's WTO accession bid back on track. The GOE and other political leaders are also working to rebuild public confidence in democratic institutions in the wake of disputed elections and unrest in ¶2005. Your visit is an opportunity to welcome the MFTR submission and highlight the benefits of WTO accession and trade liberalization in general. You will also be able to engage with senior Ethiopian officials, as well as other leaders, concerning further economic reform (see paras 7 and 8). END SUMMARY.

ECONOMIC OVERVIEW

¶2. (U) Ethiopia remains one of the poorest countries in the world. Ethiopia's GDP for 2005 is estimated at USD 8.5 billion, with an annual per capita GDP of USD 100. Since the early 1990's, Ethiopia has pursued a development strategy based on a mixed economy of both state and private enterprises. While the private sector role is expanding, the state remains heavily involved in most economic sectors, and parastatal and party affiliated companies continue to dominate trade and industry, hampering full and free competition. In addition, increasingly frequent cycles of drought, high population growth, and inefficient agricultural markets all act as a drag on Ethiopia's economic development.

Agriculture contributes 42 percent to the GDP and employs 85 percent of Ethiopia's 77 million people. Nearly all agricultural production is rain-fed and small-scale, and thus vulnerable to drought. Though GOE economic policies have been improving gradually, greater economic liberalization and reduction of population growth are critical to reducing poverty and increasing food security.

¶3. (SBU) In November 2006, the Ministry of Finance and Economic Development (MOFED) significantly revised real GDP growth rates to nearly double the IMF estimate: 11.9 percent (vice 11.6), 10.5 percent (vice 9.5), and 9.6 percent (vice 7.1) in fiscal years 2003/04, 2004/05 and 2005/06, respectively. According to the GOE, from 2003 to 2006, agriculture, industry and service sectors grew an average of 14 percent, 8.5 percent, and 8.3 percent respectively. Over 60 percent of the revised growth came from agriculture, the mainstay of the economy, contributing nearly half of the

total GDP. Major exports include coffee, oil seeds and pulses, and hides and skins, though non-traditional exports such as flowers have increased significantly over the past few years. Imports increased even faster than exports, however, resulting in a growing trade deficit and increased risk of a balance of payments crisis. The private sector has experienced some difficulty in securing hard currency for imports over the last year. Ethiopia currently has no IMF program, but the USG has urged that it establish one. The IMF has in recent months held some exploratory talks with senior Ethiopian economic officials concerning increased surveillance, though there has been no discussion of a formal program. Ethiopia participated in the enhanced Highly Indebted Poor Countries (HIPC) initiative and G8 Multilateral Debt Relief Initiative. The U.S. and Ethiopia signed a bilateral debt agreement in 2004 that provided 100 percent cancellation of Ethiopia's debt to the United States.

ECONOMIC GOVERNANCE

14. (U) There has been a great deal of progress on development of a free market economy in Ethiopia under the current government, particularly in comparison to the Military/Communist dictatorship which preceded it. There is a vibrant and growing private sector in the country; however, it is still restricted by large state ownership in the economy and involvement of "party-statal", ruling party-owned companies which dominate some key sectors of the economy. All land in the country remains state owned, although leasing arrangements for urban land are becoming more market oriented, and rural land registration is improving land tenure by providing official certificates for land use to farmers. Foreign investment restrictions are widespread, including in key sectors such as finance and

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telecommunications, but eventual liberalization is assumed as part of the WTO accession negotiation. Overall, despite some foot-dragging by the government, economic governance is making slow but steady progress.

ECONOMIC REFORM ASSISTANCE

15. (U) The USG, primarily through the U.S. Agency for International Development (USAID), supports a broad range of economic reform projects and activities. These include: WTO accession, land tenure and administration reform, improved rural economic policy, establishment of an Ethiopian commodity exchange, telecommunications, and policies related to investment and competitiveness for targeted sectors (coffee, horticulture, oilseeds/pulses, hides/skins/leather, and livestock/livestock products). Both AGOA opportunities and U.S. assistance have been effective ways to build on the GOE's strong desire to boost its exports by removing bottlenecks and promoting investments in key sectors.

16. (U) USG collaborates closely with other bilateral and multilateral donors in advancing economic policy reform and economic governance. Four donors (World Bank, European Commission, United Nations Development Program, and USAID) support Ethiopia's accession to the WTO. Five donors (Canada, Netherlands, Ireland, United Kingdom, and USAID) support the Ethiopia Strategy Support Program for rural economic policy reform. Five donors (Canada, World Bank, International Fund for Agricultural Development, United Nations Development Program, and USAID) support the Ethiopian commodity exchange initiative. USAID and Sweden support land tenure and administration reform with World Bank funding planned. Five donors support the USAID-led hides/skins/leather competitiveness cluster (Germany, United Nations Industrial Development Organization, World Bank, and USAID).

MORE REFORM NEEDED

¶7. (SBU) What else could be done in the near term? Support implementation of recommendations of the Ethiopia Commercial Law and Institutional Reform and Trade Diagnostic conducted under the USAID-funded WTO Accession Project in late 2006. Contract law, real property rights and foreign investment code liberalization are needed to significantly expand private investment and exports. Significant foreign investment is needed to expand the current cold chain facilities at Bole Airport which would increase exports of horticultural and other perishable commodities (i.e., meat). This is currently not allowed by the Ethiopian Investment Code and hindered by Ethiopian Airlines, insistence on the need to re-coup its investment in the sole cold chain facility at the airport before new facilities can be built.

¶8. (SBU) Financial sector reform is also desperately needed. Allowing foreign banks market access, relaxing requirements for letters of credit, reducing excessive collateral requirements for borrowers are among the key challenges. Customs reform is also need to streamline clearance procedures and eliminate taxation on product trade show samples. Liberalization of Ethiopia's telecommunications monopoly would also lower costs and increase quality of services across all sectors. Allowing greater private sector competition in limited areas would be a good start. The GOE has agreed to allow private sector Internet service providers and call centers, but no licenses have yet been granted. There is so far little indication that the GOE is willing to consider bold action in the financial or telecom sectors, however. There are opportunities, however, to build the advocacy role of businesses in the telecommunications sector, and to increase business development and employment opportunities through telecommunication training and development initiatives.

POLITICAL CONTEXT

SOMALIA

¶9. (U) The Ethiopian military commenced ground and air attacks against Council of Islamic Courts (CIC) targets throughout southern Somalia on December 24. The CIC structure collapsed and TFG forces routed the CIC from Mogadishu and Kismayo. Remnants of the CIC are fleeing along

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the Kenyan border or/are dispersing to meld back into their home regions. The United States released a public statement calling for all Somali parties to immediately resume peaceful dialogue and form an inclusive government based on the Transitional Federal Charter. U.S. policy in Somalia includes three goals: (1) seeking ways to help Somalia regain political and economic stability; (2) promoting counter-terrorism; and (3) alleviating the humanitarian crisis. All of these goals are being pursued in cooperation with Ethiopian, the Somali Transitional Federal Government (TFG) and other donors. The U.S. military also launched a strike Jan. 9 against members of the East Africa Al Qaeda cell believed to be on the run in a remote area of Somalia near the Kenyan border.

DEMOCRACY AND HUMAN RIGHTS

¶10. (SBU) Ethiopia is still seeking to overcome divisions and tensions that grew out of Ethiopia's disputed May 2005 elections. The elections were the freest and most contested in Ethiopian history, but irregularities in vote tabulation prompted charges of fraud by opposition groups. One of these groups, the CUD, chose to boycott public office in spite of its unprecedented gains in the elections. The party's strategy of civil disobedience drew a sharp response from the GOE in November 2005. Massive, violent public protests led to tens of thousands of arrests. While nearly all protesters

were soon released, senior 30 CUD leaders and another 50 accused "co-conspirators" from the press and civil society remain in jail on treason charges. Their trial, which international observers have witnessed, may conclude in the coming months. While the situation on the surface in Ethiopia is calm, tensions remain high.

¶11. (SBU) The U.S. has worked with all sides to pick up the pieces from the 2005 elections and move forward with democratization. There is an ongoing political dialogue between the ruling party and leaders of opposition parties that the U.S. Embassy in Ethiopia helped facilitate. Party representatives, supported by comparative studies funded by the U.S. and other donors, have negotiated reforms to strengthen the Parliament. They are currently working on similar reforms of the National Electoral Board as well as the legal framework for the media. The U.S. strategy is to press the opposition and government alike to strengthen the democratic process. Apart from nurturing talks on institutional reform, another challenge is convincing the EPRDF to further reduce harassment of opposition party activists in rural areas.

ERITREAN/ETHIOPIAN BORDER DISPUTE

¶12. (SBU) The U.S. worked closely with Ethiopia and Eritrea in 2006 to resume demarcation of the border and promote an eventual normalization of relations. The dialogue stalled, however, with Ethiopia demanding dialogue on the human impact of moving the border and Eritrea, for its part, demanding that the border simply be demarcated. According a 2006 UN report, the Eritrean government provided money, weapons, and other support to CIC extremists in Somalia who declared jihad on Ethiopia.
YAMAMOTO